UCR

Upper Canada Resources Limited

ANNUAL REPORT 1976

Upper Canada Resources Limited

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at Turbo Resources

34.14%
interest
joint co.
amalg or
acquisition

DIRECTORS:
Roy H. Allen
*Eric Connelly
*Allan H. T. Crosbie
Gerald F. Day
P. Stuart Grant
R. Michael Gray
*Ross M. Hanbury—*Chairman of the Executive Committee*
John C. McBean—*Chairman of the Board of Directors*
William A. Roliff
John N. Tilley
*H. Franklin Zurbrigg

**Member of the Executive Committee*

last Thursday.

OFFICERS:
John C. McBean
Chairman of the Board of Directors
Allan H. T. Crosbie
President and Chief Executive Officer
F. David Bignell
Vice-President, Finance
R. Michael Gray
Vice-President and Chief Geologist
Roy H. Allen
Vice-President, Oil and Gas Services
John N. Tilley
Vice-President, Mineral and Construction Drilling
Erica E. Goring
Secretary

OPERATING DIVISIONS:
OIL AND GAS SERVICES
Challenger Drilling
Challenger Drilling Inc.
Challenger Services Ltd.
Challenger Rentals Ltd.
Roy H. Allen, General Manager

MINERAL AND CONSTRUCTION DRILLING
Heath & Sherwood Drilling
Becker Drills Ltd.
Becker Drills Inc.
Becker Alaska Limited
Les Forages Becker (Quebec) Inc.
John N. Tilley, General Manager

MANUFACTURING
Drill Systems Inc.
John C. McBean, President and General Manager

AFFILIATED COMPANIES:
Bankeno Mines Limited
Belleroche Mines Limited
Queenston Gold Mines Limited
Upper Kirkland Mines Limited

TRANSFER AGENT AND REGISTRAR:
Crown Trust Company, Toronto, Ontario

AUDITORS:
Clarkson, Gordon & Co., Toronto, Ontario

HEAD OFFICE:
Suite 908, 40 University Avenue
Toronto, Ontario M5J 1T1

COVER
Rig #44—Operated by Challenger Drilling Division

Upper Canada Resources Limited
and its subsidiaries

FOUR YEAR FINANCIAL REVIEW

(unaudited—000's omitted)

	Year ended Sept. 30 1976	Year ended Sept. 30 1975	Nine months ended Sept. 30 1974	Year ended Dec. 31 1973
Operations				
Revenue	$37,215	$43,374	$21,803	$21,793
Earnings from operations	1,057	2,181	982	1,011
Gain on sale of assets	1,061	855	25	
Income before taxes and extraordinary items	2,118	3,036	1,007	1,011
Income taxes	1,130	1,568	558	538
Income before extraordinary items	988	1,468	449	473
Extraordinary items		958	523	(202)
Net Income for period	$ 988	$ 2,426	$ 972	$ 271
Earnings (loss) per share:				
Income before extraordinary items	$ 0.17	$ 0.25	$ 0.08	$ 0.09
Extraordinary items		0.17	0.09	(0.04)
Net income for period	$ 0.17	$ 0.42	$ 0.17	$ 0.05
Financial Position				
Working capital	$ 2,946	$ 576	$ (3,331)	$ (1,609)
Fixed assets (net)	$14,859	$17,146	$19,668	$14,220
Long-term debt	$ 4,879	$ 7,693	$ 9,267	$ 6,791
Shareholders' equity	$13,666	$12,678	$10,252	$ 8,323
Number of shares issued	5,740,377	5,740,377	5,740,377	5,464,827
Book value per share	$ 2.38	$ 2.21	$ 1.79	$ 1.52

TO THE SHAREHOLDERS:

For the year ended September 30, 1976, Consolidated Revenue was $37.2 million and Income before Extraordinary Items was $988,000 or 17¢ per share compared to $1,468,000 or 25¢ per share in the previous year. The 1976 results are after the Company effected a change in accounting principles regarding the valuation of inventories, reducing income after tax by $233,000 or 4¢ per share. The Company also wrote down certain inventories and fixed assets, which had the effect of reducing income after tax by $263,000 or 5¢ per share, in recognition of the continued lower levels of economic activity in the Mineral and Construction Drilling Division. In total these adjustments reduce Income before Extraordinary Items by $496,000 or 9¢ per share.

Oil and Gas Services showed an increase in revenues and earnings due to slightly increased activity. In addition, during the year the Division received $633,000 from the cancellation of a long-term drilling contract, and an amount equal to the cancellation payment has been included in depreciation in the consolidated statement of income. The other three operating divisions, namely Mineral and Construction Drilling, Manufacturing and Mining, showed substantial declines in revenues and earnings compared to the previous year resulting in the overall decline in revenues and operating earnings. Mineral and Construction Drilling was adversely affected by reduced activity in Alaska, Western Canada and Western United States. Manufacturing was adversely affected by reduced sales of drilling equipment in connection with the Alyeska Pipeline. Mining was adversely affected by the lower price of gold. There was an after-tax gain of $568,000 arising from the sale of gas leases in the North Coleman area of Alberta.

Management continues to be optimistic about the prospects for Oil and Gas Services in the coming year; this Division is traditionally the largest contributor to sales and profits. Continuing low levels of mineral exploration and delays in certain major construction projects particularly in Western Canada and the U.S.A., along with the completion of drilling activities for the Alyeska Pipeline are expected to adversely affect profits in the Mineral and Construction Drilling Division in the coming year. Also, with the completion of sales in connection with the Trans-Alaska Pipeline, Manufacturing is currently operating at a loss. Overall, therefore, the outlook for the coming year is for earnings from operations about the same or possibly slightly lower than those reported for the 1976 fiscal year.

Further substantial progress was made in the past year in improving the Company's liquidity and general financial position as evidenced by the continued improvement in working capital and the reduction in indebtedness. Over the past two years, working capital has been improved by $6.2 Million from a deficiency of $3.3 Million at September 30, 1974 to $2.9 Million at September 30, 1976, and total indebtedness has been reduced by $7.1 Million from $15.7 Million at September 30, 1974 to $8.6 Million at September 30, 1976.

34.14% interest

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acquisition

The following reviews in summary form the highlights of the main operating Divisions:

OIL AND GAS SERVICES

Challenger owns and operates 17 oil and gas drilling rigs primarily in Canada and the United States, 7 well servicing rigs in the Swan Hills area of Alberta and an oil industry related equipment rental business in Western Canada.

Of the 17 drilling rigs, 13 are located in the Yukon, British Columbia and Alberta, one in the Canadian Arctic, two in Alaska and one in Denmark. During the year, Challenger undertook a multi-well drilling program in Denmark, and in the summer of 1976 commenced drilling in the Beaufort Sea under a labour contract for Canmar Drilling, a subsidiary of Dome Petroleum. At the peak of the drilling approximately 180 personnel were employed in this operation.

MINERAL AND CONSTRUCTION DRILLING

This Division's activities are carried on through Heath & Sherwood Drilling and Becker Drills. Heath & Sherwood operates 39 drilling rigs and is engaged in mineral drilling primarily in Eastern Canada. Becker operates 25 drilling rigs and is engaged primarily in mineral and construction drilling in Western Canada and the United States.

With the completion of the Alyeska Pipeline, the Fairbanks branch has been closed and the drilling rigs relocated in the Calgary and Denver branches.

MANUFACTURING

The main products manufactured by Drill Systems Inc. are the Becker line of hammer and centre sample rotary (CSR) drills and related equipment including drill pipe, bits and accessories. Marketing of the Division's newly developed AP1000 drill, which combines the hammer and CSR drilling techniques, is in the initial stages. With the completion of

orders for the Alyeska Pipeline in May of 1976 several alternatives are being explored to restore profitability to acceptable levels.

MINING AND EXPLORATION

In August 1976, UCR terminated its agreement with Willroy Mines Limited for managing the Macassa Mine, located in the Kirkland Lake area of Ontario. The Macassa Mine operated at a breakeven level for the first nine months of the year. However, with the further decline in the price of gold in July and the prospects of continued operating losses, it was decided to terminate the agreement.

Although the decision to give up the Macassa Mine management was a difficult one in view of the Company's long history of gold mining in the Kirkland Lake area, UCR continues to maintain a number of gold mining prospects in the area. In May 1976, UCR and Queenston Gold Mines Limited, an affiliate of UCR, entered into an agreement with Canadian Nickel Company Limited, a subsidiary of Inco Limited, to undertake a gold exploration program on certain of UCR-Queenston mining claims in Gauthier and Lebel townships in the Kirkland Lake area of northeastern Ontario. Exploration is continuing on these properties.

Studies are continuing on the 100% owned Upper Beaver and Upper Canada Mine properties, and the 75% owned Belleroche Mines property, with a view to developing suitable exploration programs on these properties.

OTHER INTERESTS

UCR owns 959,448 shares of Bankeno Mines Limited, being approximately a 23% interest. Bankeno has three main interests, namely a 25% carried shareholding interest in Arvik Mines Ltd., which is operated by Cominco Ltd., approximately 1.90% share interest in Panarctic Oils Ltd. and varying interests in 2,941,483 acres of oil and gas permits in the Canadian Arctic. The net interest is 248,784 acres, most of which are farmed out to Panarctic and others. Recent drilling results by Panarctic have been encouraging. UCR continues to be optimistic about the commercial possibilities of Arvik but any commercial development of this deposit is dependent upon Cominco Ltd. and the Federal Government reaching an agreement as to satisfactory terms and conditions for development of the orebody.

Acquisition of low risk, shallow oil and gas properties in Alberta continues in partnership with Viking Oil and Gas Limited. To date, results have been encouraging.

Details of the forthcoming Annual Meeting will be contained in the Notice, Information Circular and Proxy which are being prepared separately. In any event, Messrs. A. H. T. Crosbie, G. F. Day, R. M. Hanbury and H. F. Zurbrigg will not be standing for re-election to the board. Mr. Day joined the board in 1964 and, as general counsel to the Company, has served a continuing important role in its development. Mr. Zurbrigg and Mr. Hanbury joined the board in 1974 and 1975 respectively. These three gentlemen have performed key roles in the Company, particularly over the past two years, and the Company is most appreciative of their efforts. In addition, I will be stepping down as your President and Chief Executive Officer. I very much appreciate the confidence the shareholders, directors and employees have placed in me to carry out overall responsibility for the affairs of the Company over the past two years, a period which, because of the Company's financial situation, has been particularly burdensome. I am pleased to be able to report that the problems created by this situation now appear to be substantially behind us.

In May 1976, the Company was saddened by the death of Mr. Evan T. Donaldson, a director of the Company since 1960. Mr. Donaldson was a prominent Canadian mine developer and played an important part in the development of UCR.

UCR employs between 700 and 1,000 people, depending on the seasonality of the work. Personnel are located across Canada, the United States including Alaska, and from time to time in other foreign countries. The directors extend to our valued employees sincere appreciation for their efforts and achievements.

On Behalf of the Board of Directors,

Allan H. T. Crosbie

ALLAN H. T. CROSBIE
PRESIDENT AND CHIEF EXECUTIVE OFFICER

TORONTO, ONTARIO
FEBRUARY 28, 1977

Upper Canada Resources Limited
(Incorporated under the laws of Ontario)

CONSOLIDATED BALANCE SHEET
SEPTEMBER 30, 1976
(with comparative figures at September 30, 1975)

	1976	1975
Assets		
Current:		
Cash	$ 1,372,000	$ 537,000
Accounts receivable (notes 2 and 6 (c))	7,886,000	8,856,000
Inventories (note 1 (f))	2,651,000	3,819,000
Prepaid expenses	74,000	186,000
	11,983,000	13,398,000
Investments (notes 1 (b) and 3)	1,717,000	1,748,000
Fixed assets (notes 1 (g), 4 and 6 (c))	14,859,000	17,146,000
Other (note 5)	753,000	1,668,000
Goodwill (note 1 (i))	1,133,000	1,274,000
	$30,445,000	$35,234,000
Liabilities		
Current:		
Bank loans and overdrafts (note 6 (c))	$ 1,660,000	$ 3,142,000
Accounts payable and accrued charges	5,122,000	5,981,000
Income taxes payable (note 8)	211,000	330,000
Current portion of long-term debt	2,044,000	3,369,000
	9,037,000	12,822,000
Long-term debt (note 6)	4,879,000	7,693,000
Deferred income taxes (note 8)	2,863,000	2,041,000
Shareholders' equity (note 7):		
Capital—		
Authorized:		
7,500,000 shares with a par value of $1 each		
Issued and fully paid:		
5,740,377 shares	5,740,000	5,740,000
Less discount on shares	2,330,000	2,330,000
	3,410,000	3,410,000
Contributed surplus	2,917,000	2,917,000
Retained earnings	7,339,000	6,351,000
	13,666,000	12,678,000
	$30,445,000	$35,234,000

On behalf of the Board:
A. H. T. Crosbie, Director
H. F. Zurbrigg, Director

(See accompanying notes)

Upper Canada Resources Limited

CONSOLIDATED STATEMENTS OF INCOME & RETAINED EARNINGS

YEAR ENDED SEPTEMBER 30, 1976
(with comparative figures for the year ended September 30, 1975)

	1976	1975
Income		
Revenue	$37,215,000	$43,374,000
Cost of operations	31,698,000	36,198,000
Income before the following	5,517,000	7,176,000
Interest (note 6 (d))	1,305,000	1,924,000
Depreciation (note 4)	3,013,000	2,929,000
Amortization of goodwill	142,000	142,000
Gain on sale of fixed and other assets	(1,061,000)	(855,000)
	3,399,000	4,140,000
Income before income taxes and extraordinary item	2,118,000	3,036,000
Income taxes	1,130,000	1,568,000
Income before extraordinary item	988,000	1,468,000
Extraordinary item:		
Reduction of income taxes resulting from the application of prior years' losses		958,000
Net income for year	$ 988,000	$ 2,426,000
Earnings per share (based on weighted average of shares outstanding during the year):		
Income before extraordinary item	$0.17	$0.25
Extraordinary item		0.17
	$0.17	$0.42
Retained Earnings		
Balance, beginning of year	$ 6,351,000	$ 3,925,000
Add net income for year	988,000	2,426,000
Balance, end of year	$ 7,339,000	$ 6,351,000

(See accompanying notes)

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

YEAR ENDED SEPTEMBER 30, 1976
(with comparative figures for the year ended September 30, 1975)

	1976	1975
Source of funds:		
From operations—		
Income before extraordinary item	$ 988,000	$ 1,468,000
Add (deduct) items not requiring an outlay of funds:		
Depreciation and amortization	3,155,000	3,071,000
Deferred income taxes	822,000	294,000
Loss (gain) on sale of fixed assets	45,000	(855,000)
Gain on sale of other assets	(1,106,000)	
Other		212,000
Funds provided from operations	3,904,000	4,190,000
Proceeds from sale of fixed assets	983,000	2,793,000
Proceeds from sale of other assets (note 5)	1,987,000	
Income tax recovery		958,000
Increase in long-term debt	458,000	4,713,000
Other	284,000	86,000
	7,616,000	12,740,000
Application of funds:		
Purchase of fixed assets	1,700,000	2,197,000
Reduction of long-term debt	3,272,000	6,287,000
Investments and other assets	274,000	349,000
	5,246,000	8,833,000
Increase in working capital	2,370,000	3,907,000
Working capital (deficiency), beginning of year	576,000	(3,331,000)
Working capital, end of year	$ 2,946,000	$ 576,000

(See accompanying notes)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 1976

1. Summary of significant accounting policies

(a) Basis of consolidation—

The accompanying financial statements include the accounts of the company and all of its subsidiaries.

(b) Investments—

The company uses the equity method to account for its investments in its effectively controlled companies, Queenston Gold Mines Limited and Bankeno Mines Limited.

Since both of these companies are substantially in the exploration and evaluation stage, the cost of investment approximates the underlying equity in the book value of the net assets of these companies at the dates of investment.

Other investments are carried in the company's accounts at cost.

(c) Translation of foreign currencies—

The accounts of the company's foreign subsidiaries are included in the consolidated financial statements in Canadian dollars translated as follows:

(i) Current assets and current liabilities at exchange rates in effect at the end of the year;
(ii) All other assets and liabilities at the rates prevailing when acquired or incurred; and
(iii) Operations at the average rate for the year.

Translation gains or losses are included in the consolidated statement of income and are not significant.

(d) Revenue recognition—

Drilling contract revenue and costs are accounted for on a percentage of completion basis. It is the company's policy to provide for anticipated losses on contracts in progress; no such provision was required at September 30, 1976.

(e) Demobilization costs—

Drilling contracts normally include the reimbursement of the costs of moving a rig to the drilling site, therefore, no provision is made for the costs of moving rigs at the end of contracts in progress.

(f) Inventories consist of—

	1976	1975
Drilling materials and supplies	$1,991,000	$2,734,000
Other manufacturing inventories, at lower of cost and net realizable value	660,000	1,085,000
	$2,651,000	$3,819,000

The inventories of drilling materials and supplies consist of spare parts, supplies, drill bits and drill pipe employed in the Mineral and Construction drilling operations. A substantial portion of this inventory is used and accordingly is priced at cost less amounts written off to reflect estimated usage. During the year, the company adopted the practice of expensing both stores items costing less than $10 per unit and used small tools, each of which had previously been included in spare parts at cost less amounts written off to reflect estimated usage. This change was not applied retroactively due to the difficulty in determining its effect on prior years. If this change in application of accounting principles had not been adopted, net income for the year would have increased by about $233,000 to $1,221,000 with a corresponding increase in earnings per share of $0.04 to $0.21.

This practice of including drilling materials and supplies in inventories is not followed for the Oil and Gas Services division which owns larger rigs. For Oil and Gas Services' rigs the cost of the original string of drill pipe and collars is included as part of the cost of drilling rigs and depreciated on the same basis as drilling rigs; all replacement drill pipe and collars as well as drilling materials and supplies are expensed when purchased.

(g) Fixed assets—

Drilling and manufacturing property, plant and equipment are recorded at cost. Depreciation is provided at rates designed to amortize the cost of fixed assets over their estimated useful lives, as follows:

Asset category	Depreciation method	Rate
(i) Oil and gas rigs	Standard rate per operating day which results in cost being amortized over approximately fifteen years	
(ii) Mineral and construction rigs	Substantially straight-line	10 - 20%
(iii) Automotive equipment	Substantially straight-line	20 - 25%
(iv) Portable camps	Straight-line	10%
(v) Buildings	Substantially straight-line	5%
(vi) Equipment for rent	Diminishing balance	30%
(vii) Other	Various	Various

Mining buildings, equipment and supplies are recorded at estimated realizable value which is less than original cost.

(h) Deferred mining expenditures—

All mining exploration and development expenditures are deferred until the company's properties are brought into production, sold or abandoned. These expenditures represent accumulated costs and are not intended to reflect current or future values.

(i) Goodwill—

The goodwill, all of which arose on acquisitions of subsidiaries, is amortized on a straight-line basis over ten years.

2. Accounts receivable

Details of accounts receivable are as follows:

	1976	1975
Trade	$7,818,000	$8,725,000
Due from officers and directors	68,000	131,000
	$7,886,000	$8,856,000

3. Investments (note 1 (b))

	1976 Number of shares	1976 % held of total shares outstanding	1976 Carrying value	1975 Carrying value
Bankeno Mines Limited	959,448	23	$ 941,000	$ 941,000
Advances			315,000	324,000
			1,256,000	1,265,000
Queenston Gold Mines Limited	1,056,800	22	294,000	294,000
Other			167,000	189,000
			$1,717,000	$1,748,000

The quoted market values of Bankeno Mines Limited and Queenston Gold Mines Limited, based on closing bid prices at September 30, 1976, are $1,319,000 (September 30, 1975—$1,775,000) and $285,000 (September 30, 1975—$280,000), respectively. The quoted market values do not necessarily reflect the amounts which would be realized if these shares were sold.

4. Fixed assets (note 1 (g))

Details of fixed assets are as follows:

		1976	1975
Drilling and manufacturing—			
Land		$ 394,000	$ 407,000
Buildings, rigs and other equipment	26,550,000		
Less accumulated depreciation	12,265,000	14,285,000	16,489,000
		14,679,000	16,896,000
Mining—			
Buildings, equipment, supplies and deferred expenditures		180,000	250,000
		$14,859,000	$17,146,000

During the year, the company received $633,000 on cancellation of a long-term drilling contract in the Mackenzie Delta. As some uncertainty exists concerning the future of exploration in this area, an amount equal to the cancellation payment has been included in depreciation in the consolidated statement of income.

5. Other assets

Details of other assets are as follows:

	1976	1975
Patents, at cost less amortization	$ 115,000	$ 162,000
Deferred mining expenditures, at cost (note 1(h))	290,000	282,000
Mining properties and claims, at cost less amounts written off	85,000	135,000
Oil and gas properties, at cost less depreciation	237,000	1,061,000
Other, at cost	26,000	28,000
	$ 753,000	$1,668,000

During the year, the company sold its interest in natural gas leases in the North Coleman area of Alberta and its interest in petroleum and natural gas rights in the Edwand Creek area of Alberta.

6. Financing arrangements

(a) Details of long-term debt are as follows:

	1976	1975
Term bank loans bearing interest at 2½% over the bank prime rate (1½% over U.S. base rate on $275,000 payable in U.S. dollars). These loans are due on demand; however the bank has indicated it will accept repayments of $500,000 in 1977 and various decreasing amounts thereafter to 1981 (see note 6 (c) below)	$ 1,619,000	$ 4,097,000
Term bank loan bearing interest at 1½% above the bank prime, 90% insured by the General Adjustment Assistance Board, repayable in instalments of $30,000 per month or 50% of funds generated from the operations of Drill Systems Inc., whichever is greater (see note 6 (c) below)	762,000	1,380,000
Floating charge debenture on certain of the assets of the Challenger Drilling Division of Upper Canada Resources Limited with first fixed charges on certain drilling rigs payable in monthly instalments varying from $30,000 to $40,000 plus interest at 3¼% above the bank prime rate, with a final instalment of $1,740,000 due December 1, 1978	2,688,000	3,040,000
Mortgage secured by the premises of Drill Systems Inc. due August 15, 1993, bearing interest at the rate of 11% payable in blended monthly instalments of $6,701 including principal and interest	625,000	638,000
Floating charge debenture on certain of the assets of Upper Canada Resources Limited with fixed charges on certain drilling rigs, payable June 15, 1977, bearing interest at 1% over the bank prime rate fixed on specific dates	425,000	850,000
Note secured by a chattel mortgage on certain assets of the Challenger Drilling Division of Upper Canada Resources Limited, bearing interest at the rate of 11% payable in blended monthly instalments of $5,853 including principal and interest and a final instalment of $200,000 due January, 1978	259,000	299,000
Other	545,000	758,000
	6,923,000	11,062,000
Less current portion	2,044,000	3,369,000
	$ 4,879,000	$ 7,693,000

(b) Approximate annual instalments of long-term debt in each of the five years subsequent to September 30, 1976 and thereafter are as follows:

1977	$2,044,000
1978	1,531,000
1979	2,316,000
1980	322,000
1981	171,000
Thereafter	539,000

(c) Security on bank loans:

The following have been pledged as collateral to the bank term loans, overdrafts and other bank loans:

(i) 940,740 shares of Bankeno Mines Limited;

(ii) general assignment of accounts receivable;

(iii) a $10,500,000 floating charge debenture on certain assets of Upper Canada Resources Limited, and a fixed charge on certain drilling rigs and related equipment;

(iv) a $1,700,000 floating charge debenture on the assets and undertaking of a subsidiary, Becker Drills Ltd.;

(v) a first lien on specific drilling rigs and related equipment of Becker Drills Ltd.;

(vi) a $6,500,000 floating charge debenture on the assets and undertaking of a subsidiary, Challenger Services Ltd. and a fixed charge on a specific rig and related equipment of this subsidiary;

(vii) a first floating charge on specific rigs of a subsidiary, Challenger Drilling Inc.;

(viii) a $1,500,000 floating charge debenture on the assets of Drill Systems Inc. with fixed charges on its real property and equipment and fixed charges on certain of the rigs and related equipment of Upper Canada Resources Limited;

(ix) a $400,000 floating charge debenture on the assets and undertaking of a subsidiary, Challenger Services Ltd. and a fixed charge on specific rigs and related equipment of the subsidiary.

(d) Interest expense:

Interest expense for the year ended September 30, 1976 was $1,078,000 (1975—$1,639,000) on long-term debt and $227,000 (1975—$285,000) on other debt.

7. Share capital

At September 30, 1976, a total of 259,450 of the company's shares were reserved for future issue under a stock option plan. Options granted for the purchase of 125,800 shares at prices ranging from $2.20 to $2.44 per share were outstanding at September 30, 1976, of which 62,150 are exercisable. The remaining 63,650 options become exercisable at the rate of 15,913 shares annually on or after September 30 in each of the years 1977 to 1980. All options which have not been exercised expire on December 31, 1980.

8. Income taxes

The company and its subsidiaries have available deductions which can be applied to reduce future taxable income by $984,000 consisting of (a) a loss carry forward for tax purposes of $220,000 which expires in 1978, and (b) timing differences consisting of undepreciated capital cost of $764,000 in excess of the carrying value of depreciable assets.

9. Commitments and contingent liabilities

(a) The company is committed under leases for periods varying from 1 to 6 years for total rental payments of $627,000. Rental payments for the year ending September 30, 1977 will be $169,000.

(b) An action has been brought against the company claiming damages and future compensation for alleged infringement of patents in the design of the dual wall drill pipe used in the company's operations. In the opinion of counsel, the company will be successful in its defense against this action.

(c) While testing drill pipe near its former premises located outside Fairbanks, Alaska, a subsidiary company struck what appears to be an underground water system resulting in a flow of water, causing local icing and flooding. The extent of the company's insurance coverage is unclear. However, it is the opinion of the company's legal counsel in Alaska that claims against the company arising from the icing and flooding are covered by the company's insurance policies.

No charges have been made against the 1976 consolidated income to provide for the cost of damages, if any, or for the costs of attempting to stop the flow of water.

10. Statutory information

The aggregate remuneration of directors and senior officers (as defined under The Business Corporations Act, Ontario) was $537,000 for the year (1975—$361,000).

11. Anti-Inflation Program

Under the federal government's Anti-Inflation Program (presently scheduled to be in force until December 31, 1978) the company is subject to mandatory compliance with legislation which controls prices, profit margins, employee compensation and shareholder dividends.

The operations of the company are complex and the related anti-inflation legislation and the administrative practices followed are continually being revised and clarified. In these circumstances, some uncertainties may arise from time to time and it is the company's policy to make appropriate provision for any effects of the program on the results of operations.

12. Subsequent event

Subsequent to the year-end, the company became liable to pay, to one of the senior officers, $220,000 in conjunction with his retirement from the company.

AUDITORS' REPORT

Clarkson, Gordon & Co
Chartered Accountants

To the Shareholders of
Upper Canada Resources Limited:

We have examined the consolidated balance sheet of Upper Canada Resources Limited as at September 30, 1976 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at September 30, 1976 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles which, except for the change, with which we concur, in accounting for drilling materials inventories explained in note 1 (f), have been applied on a basis consistent with that of the preceding year.

Toronto, Canada,
January 10, 1977.

Clarkson, Gordon & Co.
Chartered Accountants

(b) Approximate annual instaln

(c) Security on bank loans:
The following have been p

(i) 940,740 shares of B

(ii) general assignment

(iii) a $10,500,000 floati
rigs and related equi

(iv) a $1,700,000 floatin

(v) a first lien on specific

(vi) a $6,500,000 floating
specific rig and relat

(vii) a first floating charge

(viii) a $1,500,000 floatin
fixed charges on cer

(ix) a $400,000 floating
specific rigs and rela

(d) Interest expense:
Interest expense for the y
$285,000) on other debt.

7. Share capital

At September 30, 1976, a total o
purchase of 125,800 shares a
exercisable. The remaining 63,6
1977 to 1980. All options which

8. Income taxes

The company and its subsidiarie
loss carry forward for tax purp
$764,000 in excess of the carry

9. Commitments and contingent

(a) The company is committed
year ending September 30.

(b) An action has been brough
of the dual wall drill pipe use
action.

(c) While testing drill pipe near
ground water system result
However, it is the opinion o
covered by the company's

No charges have been mac
stop the flow of water.

10. Statutory information

The aggregate remuneration of
(1975—$361,000).

11. Anti-Inflation Program

Under the federal government's
mandatory compliance with leg

The operations of the company
revised and clarified. In these c
provision for any effects of the p

12. Subsequent event

Subsequent to the year-end, the
company.

DESIGN & CO-ORDINATION
PETER DURHAM DODD
TORONTO

Upper Canada Resources Limited
Suite 908—40 University Avenue, Toronto, Ontario M5J 1T1
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UPPER CANADA RESOURCES LIMITED
and its subsidiaries

Consolidated Statement of Changes in Financial Position
Six Months Ended March 31, 1976
(with comparative figures for 1975)
(unaudited)

	1976	1975
Source of Funds:		
From operations —		
Net income for the period	$1,659,000	$1,345,000
Add (deduct) items not requiring an outlay of funds:		
Depreciation and amortization	1,755,000	1,478,000
Deferred income taxes	156,000	747,000
Gain on sale of assets	(1,035,000)	(391,000)
Funds provided from operations	2,535,000	3,179,000
Proceeds from sale of fixed assets	523,000	1,125,000
Proceeds from sale of other investments	2,130,000	(27,000)
	5,188,000	4,277,000
Application of Funds:		
Purchase of fixed assets	789,000	1,484,000
Reduction in long-term debt (net)	2,366,000	(1,053,000)
	3,155,000	431,000
Increase in working capital during period	2,033,000	3,846,000
Working capital, beginning of period	576,000	(3,331,000)
Working capital, end of period	$2,609,000	$ 515,000

Printed in Canada

UCR

Interim Report

for the six months ended March 31, 1976
(unaudited)

UPPER CANADA RESOURCES LIMITED
SUITE 908, 40 UNIVERSITY AVENUE
TORONTO, CANADA
M5J 1T1

To the Shareholders:

For the six months ended March 31, 1976 revenue was $20,821,000 and net income after taxes was $1,659,000 or 29¢ per share. Of this amount, $562,000 represented gain on sale of assets after taxes. Income from operations after taxes amounted to $1,097,000 or 19¢ per share compared to 18¢ per share in the previous year.

For the six month period Oil and Gas Services (Challenger) showed a substantial increase in operating earnings compared to the corresponding period in the previous fiscal year. The outlook continues to be favourable for this Division. Mineral and Construction Drilling (Heath & Sherwood and Becker) showed a modest profit. Manufacturing (Drill Systems) reported good profits in line with last year's results, mainly from sales in connection with the Trans-Alaska Crude Oil Pipeline. The substantial portion of these orders have been completed. Mining (Macassa Gold Mine) continues to operate at a breakeven level, down from the profits of the previous year.

Since Oil and Gas Services is a major contributor to the Company's earnings and is seasonably most active during the winter, the first six months can be expected to account for the substantial portion of the Company's annual earnings.

In May, it was announced that UCR and Queenston Gold Mines Limited had entered into an agreement, subject to certain conditions, with the Canadian Nickel Company Limited, a subsidiary of Inco Limited, to undertake an exploration program on certain of UCR's and Queenston's mineral claims in Gauthier and Lebel townships in the Kirkland Lake area of north-eastern Ontario. UCR and Queenston have agreed to exchange certain of their interests in the properties so that the overall interest in the claims in the area to be explored will be held 25% by UCR and 75% by Queenston.

ALLAN H. T. CROSBIE,
President and Chief Executive Officer.

Toronto, Ontario,
May 28, 1976.

File

UPPER CANADA RESOURCES LIMITED
and its subsidiaries

Consolidated Statement of Income
For the Period Ended March 31, 1976
(with comparative figures for 1975)
(unaudited)

	SIX MONTHS		THREE MONTHS	
	1976	1975	1976	1975
Revenue	$20,821,000	$23,906,000	$12,880,000	$15,496,000
Cost of operations	15,875,000	19,445,000	9,601,000	12,631,000
Income before the following	4,946,000	4,461,000	3,279,000	2,865,000
Interest	773,000	976,000	339,000	476,000
Depreciation	1,684,000	1,478,000	1,157,000	894,000
Amortization of goodwill	71,000		36,000	
Gain on sale of assets	(1,080,000)	(368,000)	(1,080,000)	(368,000)
	1,448,000	2,086,000	452,000	1,002,000
Income before taxes	3,498,000	2,375,000	2,827,000	1,863,000
Income taxes	1,839,000	1,030,000	1,475,000	753,000
Net income for period	$ 1,659,000	$ 1,345,000	$ 1,352,000	$ 1,110,000
Earnings per share:				
Net income for period	$.29	$.23	$.24	$.19